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Japan's Economy Maintains Rapid Growth In 1990 But Worries Mount

The Japanese economy continued to shine brightly in 1990, but by yearend the light seemed noticeably dimmer. The gross national product expanded a price-adjusted 5.6 percent last year, which represented an acceleration from the 4.7 percent pace achieved in 1989 (see Table). But the October-December quarter saw growth slow to an annualized rate of only 2.1 percent. Domestic demand alone would have produced 5.8 percent overall growth in 1990, but foreign trade shaved 0.2 percentage point off this rate, the fifth straight year in which net exports were a drag on the economy. The current account as a percentage of nominal GNP declined to 1.2 percent last year compared to 2 percent in 1989 and a peak value of 4.2 percent in 1986.

The 1990 GNP results were far better than expected by most analysts a year ago. The main reason was plant and equipment spending, which jumped 13.7 percent in real terms and accounted for nearly half of the overall expansion. Such spending accounted for 19.7 percent of nominal GNP, the highest figure in 20 years. (For more details, see JEI Report No. 11A, March 22, 1991.) Firm

Japan's Real Gross National Product at Constant (1985) Prices

(in billions of yen, seasonally adjusted, quarterly totals and rates of growth at annual rates)

	1989	1990	January-March 1990	April-June 1990	July-September 1990	October-December 1990
Gross National Product	Y383,092.8 (4.7%)	Y404,524.2 (5.6%)	Y397,447.8 (6.6%)	Y402,877.4 (5.6%)	Y407,432.8 (4.6%)	Y409,539.2 (2.1%)
Personal Consumption Spending	223,296.8 (4.4%)	232,221.4 (4.0%)	229,493.1 (1.3%)	233,094.6 (6.4%)	233,453.1 (0.6%)	232,790.4 (-1.1%)
Private Residential Construction	21,661.4 (0.1%)	23,581.1 (8.9%)	22,080.3 (5.5%)	23,238.8 (22.7%)	24,616.2 (25.9%)	24,217.5 (-6.3%)
Private Fixed Nonresidential Investment	76,512.9 (15.6%)	87,025.4 (13.7%)	83,429.0 (15.2%)	85,923.6 (12.5%)	87,867.2 (9.4%)	90,577.4 (12.9%)
Change in Business Inventories	3,684.3 (14.5%)	2,914.3 (-20.9%)	2,180.7 (*)	3,348.8 (*)	3,512.8 (*)	2,607.9 (*)
Government Current Expenditures	33,510.3 (2.1%)	33,974.5 (1.4%)	33,901.9 (3.1%)	33,902.0 (0.0%)	33,945.9 (0.5%)	34,151.5 (2.4%)
Government Fixed Investment	25,042.6 (-1.2%)	25,917.5 (3.5%)	25,697.3 (6.5%)	25,958.5 (4.1%)	26,018.8 (0.9%)	26,040.6 (0.3%)
Change in Government Inventories	-87.6 (*)	128.2 (*)	203.4 (*)	433.5 (*)	603.0 (*)	-724.7 (*)
Net External Sector	-527.8 (-118.2%)	-1,238.3 (*)	462.1 (*)	-3,022.4 (*)	-2,584.2 (*)	-121.4 (*)
Exports of Goods and Services and Factor Income Received	65,779.2 (15.0%)	72,844.9 (10.7%)	73,636.7 (29.9%)	74,052.7 (2.3%)	70,837.4 (-16.3%)	72,870.7 (12.0%)
Imports of Goods and Services and Factor Income Paid	66,307.0 (22.1%)	74,083.1 (11.7%)	73,174.6 (12.4%)	77,075.1 (23.1%)	73,421.6 (-17.7%)	72,992.1 (-2.3%)

*Cannot be calculated or meaningless.

Source: Economic Planning Agency

continued to invest in new plant and equipment during the second half of the year; otherwise, businesses and consumers became more cautious. Between July and December, GNP growth on an annualized basis slowed to 4.2 percent from the 6 percent pace of 1990's first half. The last three months of the year were the worst of all. Even in the fourth quarter, however, plant and equipment spending remained strong, rising 12.9 percent from the previous quarter on an annualized basis.

The only other important source of growth in the fourth quarter was the foreign sector. Real exports grew 12 percent, while price-adjusted imports shrank 2.3 percent. (The figures do not imply that Japan's current account surplus, as usually measured, increased. In fact, the imbalance declined 30.9 percent in the fourth quarter from a year earlier.) The resulting gain in net exports contributed 0.6 percentage point to the quarterly growth rate, which came in at 0.5 percent. In other words, without help from foreign trade the value of Japanese output would have declined modestly, other factors equal. Had both business investment and the external sector been neutral, the economy would have shrunk 3.2 percent in real terms on an annualized basis in the fourth quarter.

In discussing the economy's prospects analysts tend to weigh the potential for weaker plant and equipment spending and reduced net exports against the likelihood of a rebound in the rest of the economy. Unfortunately, the odds of the first scenario unfolding are much better than those of the second. An increasing number of experts believes that business investment is likely to slow dramatically over the next year, a result of higher interest rates and poor prospects for profitability. The same analysts expect export growth to be sluggish as a result of the worldwide economic slowdown.

Consumer spending, which the Economic Planning Agency said turned in a dismal October-December performance because of warm weather, is likely to rebound a little, but it is not expected to be strong enough to carry the economy. Despite appropriately cold weather, however, real household spending in January, the most recent month for which data are available, was a scant 0.1 percent ahead of a year earlier as consumer confidence remained shaky. Housing also is unlikely to pick up the slack; it probably will remain in the doldrums as long as interest rates remain high by historical standards. The data clearly reveal a temporary surge in housing investment in the middle of 1990 as potential home buyers hurried to outrace surging interest rates. This pattern suggests that housing starts last year could have been borrowed from future periods, yet another reason for pessimism concerning 1991.

If, given current conditions, the private domestic and foreign sectors are unlikely to provide much spark, then only government could provide a jump start. The most obvious alternative is lower interest rates, which could boost capital spending in the business sector and prop up the housing market. Some government and Liberal Democratic Party officials have pushed the Bank of Japan to take action, but BOJ appears to be biding its time. The bank routinely and strongly has denied recent rumors that it plans to reduce the official discount rate, stuck at 6 percent since last August 31. The central bank, in fact, still has its foot on the brake. By reducing the growth of the money supply to only 5.4 percent on a year-to-year basis in February -- the lowest rate of expansion since current yardsticks were adopted in 1979 -- BOJ has moved to tighten monetary policy and to put upward pressure on short-term rates.

Fiscal policy -- the use of government spending and taxation to affect the growth rate of the economy -- is an even less likely candidate to increase economic growth. The 1990 GNP figures, which show real government spending growing less rapidly (2.3 percent) than business and consumer outlays, could be interpreted to mean that the economy could put more spending to good use. However, price increases on the goods and services purchased by the government were greater in 1990 than for the economy in general. This result suggests that higher government expenditures could worsen inflationary pressures significantly, a major worry in an economy where the labor supply remains extremely tight.

In short, the Japanese economy appears virtually assured of slower growth in 1991 than it recorded in 1990. If, as analysts expect, real GNP expands at least 2 percent and perhaps as much as 4 percent, the economy's performance would still be impressive given the tight labor market, which limits potential growth severely. In addition, Japan's GNP is likely to expand faster in 1991 than that of the United States and other industrialized countries, where growth could be flat. These considerations imply that, despite being somewhat dimmer than in 1990, Japan's economic star is likely to appear relatively bright in 1991's darker economic firmament.

Douglas Ostrom

All Japan Watches Wage Talks

The annual nationwide negotiations between labor unions and companies over wage increases has been an important event on Japan's political and economic calendar since their inauguration after the end of World War II. The spring wage offensive, or shunto, directly affects workers' pocketbooks and companies' bottom lines and indirectly affects the entire economy through these two channels. This year's shunto, however, is being watched with particular interest by fiscal and monetary policymakers because the wage talks are taking place against a background rife with economic uncertainties. Most analysts believe that a number of circumstances will collude to limit wage increases to levels no higher than last year's and very possibly below 1990's average increase of 5.94 percent.

As is customary, maneuvering by labor and management representatives began months before the March 10 opening of direct wage talks. Workers initially felt they were in a strong position to win bigger wage hikes than last year's because the economic expansion looked unstoppable. Neither plunging share prices on domestic stock markets nor the slowing U.S. economy seemed to put a dent in private capital investment or consumer spending, the twin pillars of the current boom. Unions began laying the groundwork for wage increases of 8 to 9 percent.

Developments soon proved the Japanese economy is mortal. The Bank of Japan's credit squeeze and the events triggered by Iraq's invasion of Kuwait all began to shake consumer and corporate confidence. Price-adjusted economic growth in the last quarter of 1990 dropped to a 2.1 percent gait on an annualized basis (see preceding article). Many business leaders worry that if wages grow faster than the government's projected 3.8 percent rate of real growth in FY 1991, the resulting inflation could force the economy to sputter to an even slower pace. Employers have come to the conclusion that a wage hike equal to last year's is out of the question; they have set their sights on a pay increase of just 2.5 percent.

NOTE

ONLY THE FOLLOWING PAGES OF THIS

PUBLICATION HAVE BEEN FILMED

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